JPMorgan

Australia and New Zealand - Weekly Prospects

Summary

- Minutes from the **RBA's** monetary policy meeting released last week showed that Board members considered hiking interest rates 50bp at their February meeting. The RBA decided to hike the cash rate 25bp on February 5, but debated the need for a larger move. The labour price index last week showed that wage growth picked up in 4Q, rising 1.1%q/q. This week's capital expenditures survey will likely show business investment rebounded in 4Q. Solid business investment should help boost productive capacity and alleviate pressure on stretched resources which should, eventually, assist in curbing inflation. The RBA's private sector credit aggregates on Friday will probably show credit growth eased in January.

- In what was a relatively quiet week in **New Zealand** on the economic data front last week, the ASB housing confidence survey showed that optimism on the direction of house prices continued to weaken. The sharp downturn in the housing market, coupled with the recent drought, are likely to be the two key developments in the RBNZ's rhetoric, which will be painted in the next monetary policy statement on March 6. In other data, electronic card spending showed a substantial 0.6%m/m drop in spending on core retail goods (excluding vehicle-related industries). Higher petrol prices and rising interest rates are taking their toll.

- The most immediate concern facing the **global economy** is the fallout from a potential US recession. The resulting sustained contraction in profits and labour income would magnify stress in credit markets that are already impaired. A US recession also would likely spill over to parts of the global financial marketplace that have, as yet, remained relatively unharmed. At present, US growth appears to be stalling, but the economy has shown little sign of a pronounced shift in business and household behaviour that would mark the onset of recession. To be sure, the economy is on a razor's edge, and household purchasing power appears to be getting less relief than expected this quarter from food and energy prices. In addition, continued widening in credit spreads is thwarting the transmission of Fed easing to private sector borrowing rates.

- In the US, **policymakers'** aggressive actions to offset recession risks make sense, given the potential for large adverse consequences of a negative feedback loop between growth and credit market stress. Chairman Bernanke is likely to emphasize this risk in this week's testimony, laying the groundwork for additional easing next month. If the US economy is sliding into recession, policy actions that will deliver a large midyear tax rebate and a zero real funds rate will provide a sizable cushion in 2H08. However, if the US economy skirts recession, policy will add to growth as the drags fade from energy prices increases, declining residential construction, and inventory drawdowns. In this case, the stage will be set for US growth to move above 3% in 2H08, while keeping core inflation well above the top of the Fed's comfort zone.

This week's highlight

In Australia, private capital expenditure numbers are scheduled for release on Thursday. Business investment will likely rise 6.0%q/q in 4Q, after falling unexpectedly in the previous quarter.

Contents

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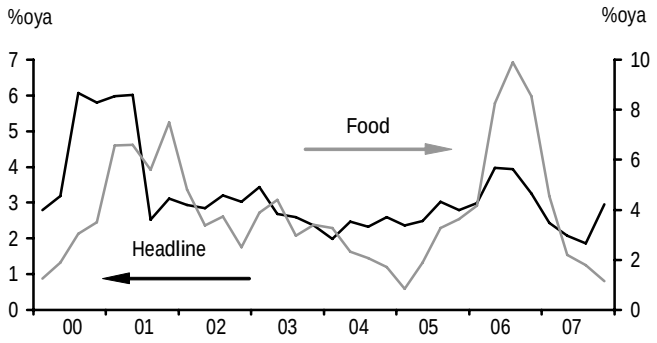
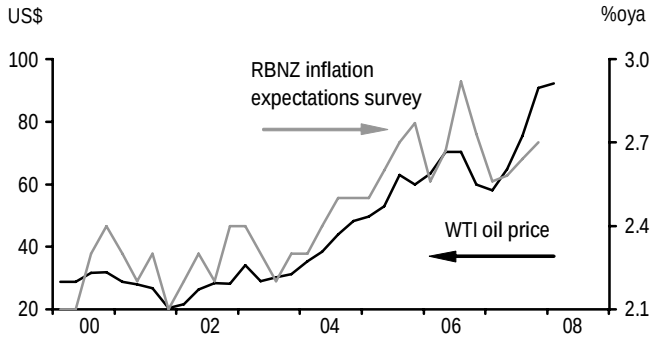
This week's feature charts

Australia: rising food prices add to inflation



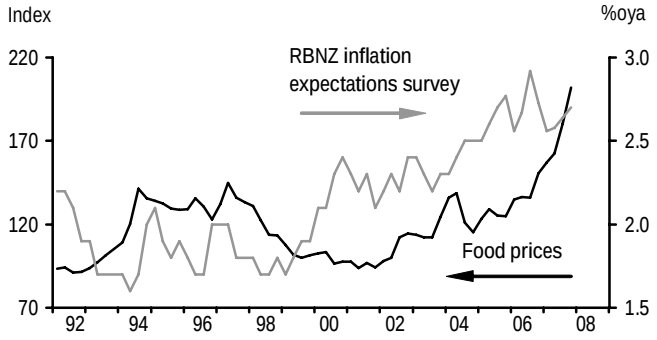
The RBA released a report on February 21 acknowledging, among other things, that food price increases in recent years have outpaced overall inflation. The report suggested that the outlook for domestic food prices this year will depend largely on local rainfalls. It also noted, though, that global food price inflation may continue to put upward pressure on domestic prices, as the prices of food exports and imports rises.

New Zealand: WTI oil price and inflation expectations



There is a strong correlation between rising petrol prices and inflation expectations. The WTI breaking through US$100 last week, and the expectation of higher petrol prices down the line, will only add to consumer fears and inflation expectations in the near term.

New Zealand: Economist food price index and inflation expectations



The global rise in food prices is not about to revert. This staggering climb in food prices has been driven by both greater demand and reduced supply. The demand-side shock can be largely attributed to the growing appetites of the rapidly expanding Chinese middle-class. The supply-side shock has been due to an extended drought in Australia (and now NZ), increased land allocation for biofuels, and changes to farm subsidies in Europe. The rise in food prices is pushing up inflation expectations.

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Economic Research note

Fiscal policy targeting lower inflation in Australia

- **Fiscal policy to play key role in macroeconomic management, particularly inflation targeting**
- **Significant government spending cuts expected in federal budget in May**
- **A terms of trade correction, although unlikely, could result in a budget deficit, and increased bond issuance**

In response to building inflation pressures, Australia's newly elected Labor government last month announced a five-point plan to fight inflation. Annual core inflation is hovering well above the RBA's 2-3% target range, and is forecast by the RBA to remain uncomfortably high for at least the next two years. Spending cuts and additional savings of more than A$10 billion identified during last November's election campaign are key to the government's plan to curb inflation, which it believes is its primary challenge in the first three-year term of government.

Budget restraint key to fighting inflation

Key to Labor's inflation fighting plan is cutting government spending. A budget surplus of 1.5% of GDP has been targeted in 2008-09, up from 1.0% targeted by the previous Coalition government. The government already has announced A$643 million of spending cuts, focused mainly on reversing promises made by the former administration.

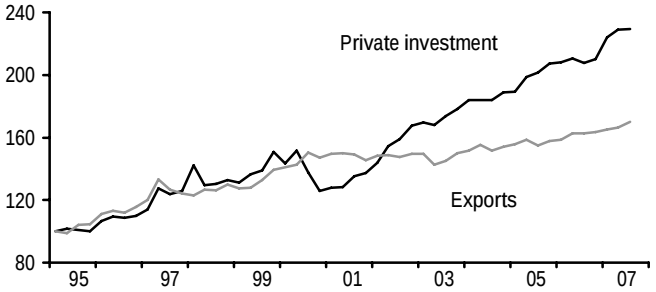
The other four parts of Labor's inflation fighting plan are:

- **incentives to encourage private saving** via, for example, first home saver accounts. Households have saved, on average, none of their disposable incomes since 2000;
- **tackling the chronic skill shortage**. Another 20,000 training places have been made available under the government's 'Skilling Australia for the Future' plan;
- **alleviating infrastructure bottlenecks.** A statutory body called Infrastructure Australia will address chronic underspending on roads, ports, and railways; and,
- **boosting work force participation** by helping people reenter the work force, via practical measures such as boosting affordable child care and removing other disincentives to returning to work.

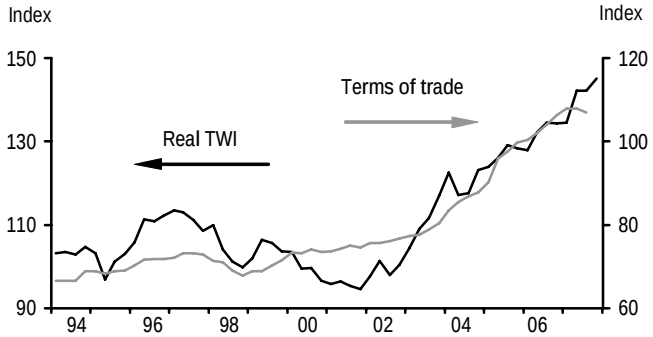
The measures will not immediately counter building inflation

Business investment to increase capacity

Constant prices, 1995=100



Real effective exchange rate and terms of trade



pressures. The fiscal tightening will have to stem largely from even deeper spending cuts given Labor has pledged to deliver the generous income tax cuts promised in the election campaign. Not doing so in the government's first term would be committing political suicide.

Tax cuts to add further fiscal stimulus

Labor has pledged to deliver A$31 billion in tax cuts over the next three years, in the face of a deteriorating inflation outlook that suggests that this is economically irresponsible. When discussing the inflation outlook in its quarterly Statement on Monetary Policy, the RBA attributed solid household income growth to strong employment gains, rising real wages, and income tax relief. Although the statement did not refer directly to the government's planned tax cuts, five straight years of income tax cuts have undoubtedly stimulated private demand to a greater extent than rising interest rates have tempered it, fanning inflation.

Indeed, the anticipated fiscal stimulus comes at a time when the economy is calling out for restraint. The RBA recently lifted its inflation forecasts to above the 2-3% target range out to 2010. Labor, not surprisingly, has come under significant pressure to defer the tax cuts, or direct at least some of them into superannuation accounts to curb building inflation pressures. The government argues, though, that planned tax cuts

will not be inflationary, and will encourage greater work force participation by providing incentives for people to return to work, and encouraging skilled migration. In 2007, Treasury Secretary Ken Henry estimated that tax cuts could lift labour supply about 0.1 hour a week. Increased labour supply and higher participation would help limit wage growth, easing some upward pressure from inflation.

Terms of trade to fuel even bigger surplus

Expansionary fiscal policy during the long resource boom has made the task of curbing inflationary pressure more difficult. The terms of trade has surged 40% over the last four years. This helps to explain why real domestic income and nominal GDP have risen steeply, and company profits have skyrocketed, fuelling faster import growth and higher production. The widening gap between real domestic income and production fuelled inflation, inflation which strong AUD could only partially offset.

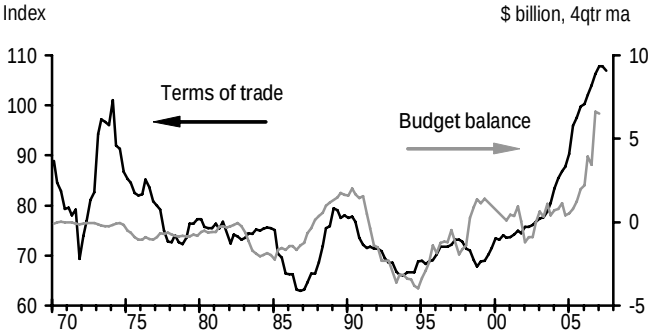
The rise in company profits led resource companies to invest in new projects and expand production. Solid business investment—which, as a proportion of GDP, is at a record peak—and capital deepening should continue to lift productivity growth, which has been on a structural decline since the 1990s. Investment has reached a mature phase and the increase in capacity and productivity growth anticipated should help dampen inflation.

But, the terms of trade is on track to hit new record highs in 2008, making even more economic stimulus likely. JPMorgan's forecasts iron ore contract prices to rise 65%, owing to continued robust demand from China, where steel production is growing rapidly and iron ore production is slowing. Coal contract prices are expected to roughly double and, according to our forecasts, thermal coal and coking coal contract prices will jump over 60% and 40%, respectively. In some cases, this is greater than the 40-50% rise in contract prices forecast for major commodities by the RBA, so the 5% boost to the terms of trade anticipated by the RBA probably will be surpassed. A further rise in terms of trade would help provide the government scope to target an even larger budget surplus.

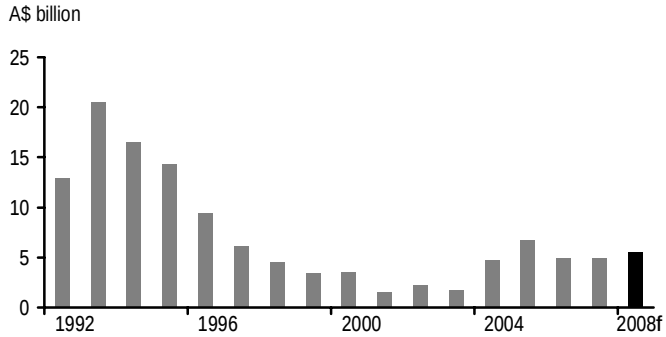
Higher bond issuance if targets not met

That said, a terms of trade correction is a growing risk beyond 2008. The terms of trade is strongly correlated with global GDP growth, the outlook for which has rapidly deteriorated in recent months.

Terms of trade bolsters budget surplus



Gross new issuance of Australian government bonds



A sustained correction in the terms of trade even could lead to budget deficits, the threat of which would encourage the government to make even deeper spending cuts, as it probably would not have the luxury of being able to rely on positive shocks like the resource boom to generate revenue. A deficit probably would result in greater government bond issuance. In 1993, for example, the fiscal deficit of 6% of GDP was met with government bond issuance of more than A$20 billion, a small portion of which was issued solely to maintain market liquidity. Despite having run surpluses since 1997, ignoring a small deficit in 2001, the government has issued around A$5 billion in bonds each year to maintain market liquidity. Issuance became a function of managing liquidity rather than budget funding, especially following the elimination of net debt in 2006.

Low bond issuance can make it harder for the RBA to carry out normal market operations. When demand for money outweighs supply, the RBA supplies funds to the banking system to ease upward pressure on the cash rate target. To do this, it buys government bonds from private holders, but low bond issuance can make it harder for the RBA to find counterparts with enough securities to offer. Greater bond issuance, therefore, could grease the wheels for the RBA.

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Australia

- **February minutes show RBA considered 50bp hike**
- **Wage growth accelerated to 1.1%q/q in 4Q**
- **Private sector credit growth to slow in January**

Minutes from the RBA's monetary policy meeting released last week showed that Board members considered hiking interest rates 50bp at their February meeting. The RBA decided to hike the cash rate 25bp on February 5, but debated the need for a larger move. The labour price index, meanwhile, showed that wage growth picked up in 4Q. This week's capital expenditures survey will likely show business investment rebounded in 4Q, while the RBA's private sector credit aggregates will probably show credit growth eased in January amid rising interest rates.

Capex to rebound in fourth quarter

The 4Q business survey is expected to show that capital spending rebounded 6.0%q/q, after falling 6.5% in the previous quarter. Investment unexpectedly fell across each of the main industry groups in 3Q—mining (-3.0%), other selected industries (-9.3%), and manufacturing (-2.1%)—as some firms struggled to acquire the required labour and equipment to undertake planned investment projects.

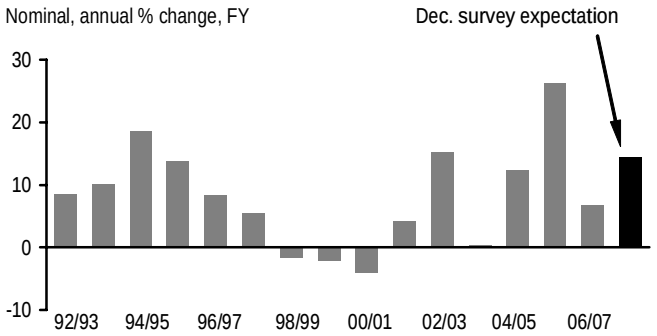
More importantly, the forward looking component of the 3Q survey showed that firms downgraded expectations for spending in the year ending June 2008 to a still-healthy 14%, from 17% previously. The downgrade probably reflected growing uncertainty over the global growth outlook, tightening credit conditions, and rising domestic interest rates.

Solid business investment should help boost productive capacity and alleviate pressure on stretched resources which should, eventually, help curb inflation. That said, while business investment is growing at healthy double-digit pace, the current investment cycle is at a very mature phase, and spending will probably start to moderate in coming quarters.

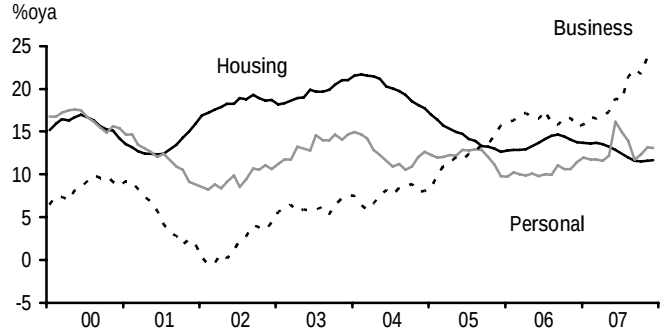
Credit growth to hold steady in January

Private sector credit is forecast to grow 1.0%m/m in January, slowing from 1.1% in December. The annual growth rate will fall to 16.3% from 16.5%, which was the highest level since 1989. This moderation will be welcomed by the RBA given that credit growth has been accelerating in annual terms even though the central bank lifted rates in August and November.

Australia: business investment



Australia: private sector credit aggregates



In January, business lending will again underpin total credit growth. Presumably, lending by businesses will be used to fund investment in additional capacity and help alleviate infrastructure bottlenecks. Personal and housing credit growth, in comparison, will appear soft, and probably will slow under the weight of the RBA's November rate hike and the rise in banks' standard variable mortgage rates—outside of an RBA rate hike—in early January. While lending by corporates is move favourable than excessive credit inflated by household borrowing, the RBA will remain anxious that credit continues to expand so rapidly.

RBA considered 50bp move in February

Minutes from the RBA's February monetary policy meeting last week showed, among other things, that RBA officials considered hiking interest rates 50bp at their last meeting. The RBA decided on February 5, however, to hike the cash rate 25bp to a 12-year high of 7%.

RBA officials debated whether to raise the cash rate 25bp or 50bp in early February. The argument in favour of a 50bp move stemmed from the deteriorating inflation outlook. The Board acknowledged also that the cash rate in real terms was

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relatively low given current domestic economic fundamentals. A 25bp hike was judged "more persuasive", however, given several domestic banks had lifted their borrowing rates in recent months in the absence of a rise in the official cash rate. Furthermore, the RBA decided that further tightening could be implemented in March, or thereafter, if policy was judged not restrictive enough. JPMorgan forecasts that the RBA will hike interest rates 25bp in March and May.

The Board also discussed the weakness in the US economy, particularly in the housing sector, noting that this weakness could spread to other sectors as growth in incomes and spending fell. Other developed economies, such as Japan, had softened, but developing countries, like China, were performing well. On financial markets, the RBA noted ongoing turbulence in currency and equity markets, further write downs by financial institutions, and rising pessimism about the global growth outlook. The RBA discussed the policy responses of other central banks to recent global developments, noting policy easing in some developed countries and tightening in some emerging markets.

On the domestic economy, the Board discussed recent data on businesses, households, the housing market, credit growth, trade, and the labour market. The RBA forecast that GDP growth will slow to 3.25% by the end of 2008. On inflation, RBA officials noted that price rises in the past two years have been broad based, with both prices of non-tradable and tradable items rising. It forecast, though, that underlying inflation would rise to 3.75% in early 2008 and decline gradually to 3% by mid-2010—holding at the very top end of the bank's 2-3% target range.

RBA's Edey maintains hawkish bias

RBA assistant governor Malcolm Edey, in a speech to the Committee for Economic Development of Australia on Tuesday, reiterated comments recently made in the bank's quarterly Statement on Monetary Policy, which reaffirmed widespread expectations that interest rates will rise further.

Mr. Edey acknowledged that the housing-driven slowdown in the US economy was feeding back into employment and incomes, but noted several positive forces likely to support US economic growth going forward—the weak US dollar favouring exports; the significant fiscal stimulus in the pipeline; and falling interest rates. Mr. Edey suggested also that the current weakness in major industrial economies would have a dampening effect on the Asian region, and forecast that growth in Australia's trading partners will slow to a below-trend 4% in 2008 and 2009, down from 5% last year, mainly due to weak growth in G7 economies. He restated, though, that the weakness in developing countries, such as China, was less pronounced, and noted firm conditions in other Asian economies.

RBA output and inflation forecasts

%oya

	GDP	Consumer price index	Underlying inflation
Sep-07	4.30	1.90	3.00
Dec-07	3.50	3.00	3.60
Jun-08	3.25	3.50	3.75
Dec-08	3.25	3.50	3.50
Jun-09	3.00	3.25	3.25
Dec-09	3.00	3.25	3.25
Jun-10	3.00	3.00	3.00

Source: RBA, ABS

Australia: labor price index and unemployment

Mr. Edey said that economic growth in Australia remains robust and will likely be sustained. In particular, the terms of trade will remain a significant stimulus to the domestic economy, with the RBA forecasting that the terms of trade will rise another 5% this year. Strong demand and tight capacity, rising commodity prices, and faster wages growth, will continue to fan inflation, however. The RBA forecasts the underlying trend in inflation is now around 3.5%, and remains concerned that rising inflation might feed back into domestic wage and price expectations.

Wage growth accelerates in 4Q

Wage growth picked up in 4Q, with the labour price index

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rising 1.1%q/q (JPMorgan 1.2%, consensus 1.1%), up from 1.0% in 3Q. Annual wage growth held steady at 4.2% for the second straight quarter, as private sector wages picked up (+4.3%) and public sector wage growth eased (+4.1%).

Persistently tight labour market conditions, widespread skill shortages, and anecdotal evidence suggesting that labour costs are rising, means that wage growth will likely accelerate in coming quarters. The threat of additional wage cost pressure is something the RBA clearly is concerned about. The February monetary policy minutes highlighted the tight labour market, but noted that wage growth to date had surprisingly remained contained. The RBA pointed out, though, that average earnings from the national accounts had showed a significant pick up in wage growth, which we expect will be illustrated by a gradual increase in the labour price index in coming quarters.

Australia:
Data releases and forecasts

Week of February 25 - 29

Wed Feb 27 11:30am — **Construction work done**
Seasonally adjusted

	1Q07	2Q07	3Q07	4Q07
(%q/q)	3.6	-2.1	2.8	__
(%oya)	10.2	3.0	8.9	__

Thu Feb 28 11:30am — **Private new capital expenditure**
Seasonally adjusted

	1Q07	2Q07	3Q07	4Q07
(%q/q)	9.4	7.1	-6.5	6.0
(%oya)	4.5	11.8	9.0	16.1

Fri Feb 29 11:30am — **Private-sector credit**
Seasonally adjusted

	Oct	Nov	Dec	Jan
(%m/m)	1.0	1.7	1.1	1.0
(%oya)	15.4	16.2	16.5	16.3

Review of past week's data

WMI leading index
Seasonally adjusted

	Oct	Nov		Dec	
(%m/m)	0.5	~~1.0~~	*0.9*	__	*-0.2*

Labour price index
Seasonally adjusted

	2Q07	3Q07	4Q07	
(%q/q)	1.1	1.0	~~1.2~~	*1.1*
(%oya)	4.0	4.2	~~4.3~~	*4.2*

Sales of new motor vehicles
Units, seasonally adjusted

	Nov	Dec		Jan	
(%m/m)	1.5	~~1.1~~	*1.6*	__	*0.6*
(%oya)	10.6	~~11.6~~	*11.7*	__	*7.2*

New Zealand

- **RBNZ inflation expectations to worsen this week**
- **Housing market confidence sliding deeper into darkness**
- **PPI report still points to inflation pressure in pipeline**

In what was a relatively quiet week in New Zealand on the economic data front last week, the ASB housing confidence survey showed that optimism on the direction of house prices continued to weaken. The sharp downturn in New Zealand's housing market, coupled with the recent drought, are likely to be the two key developments in the RBNZ's rhetoric, which will be painted in the next monetary policy statement on March 6. In other data, electronic card spending showed a substantial 0.6%m/m drop in spending on core retail goods (excluding vehicle-related industries). Higher petrol prices and rising interest rates are taking their toll.

RBNZ inflation expectations on the rise

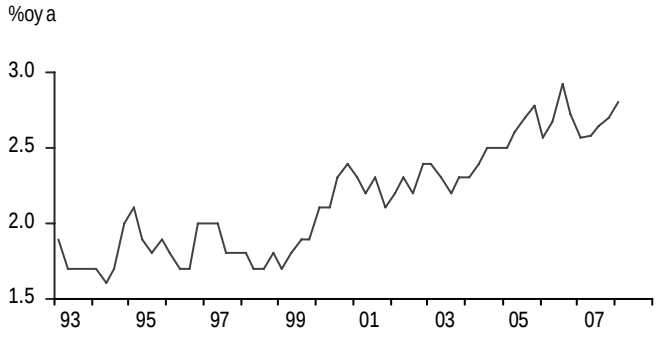
The RBNZ inflation expectations survey, out Tuesday, should gather some interest in the market. Inflation expectations is a major input in the RBNZ's inflation model, and expectations are likely to have risen in 1Q. Inflation expectations tend to track oil and food prices, both of which have increased substantially in recent months. Rising inflation expectations will worsen the inflation outlook, and keep the possibility of an interest rate cut off the table.

That said, whilst the inflation trajectory will keep RBNZ officials on guard, the chances of a further rate rise in this cycle are diminishing by the day. New Zealand's housing market has turned south harder and faster than RBNZ forecasts, and an unfortunate drought in New Zealand's major dairy producing regions is taking a slice out of growth in export volumes. We expect the RBNZ to downwardly revise its housing market forecasts in the March quarter monetary policy statement to reflect a slight decline in house prices—somewhere in the order of -5% in 2008—and a minor cut in export volumes growth.

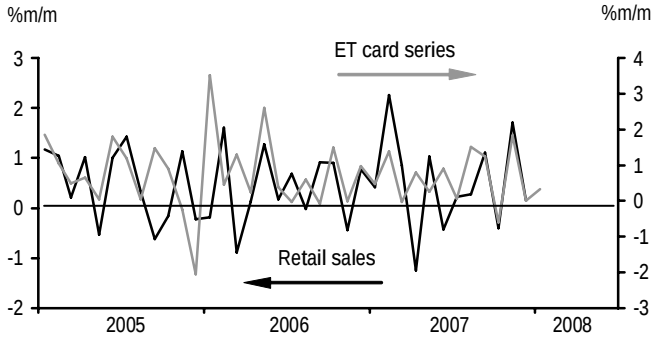
Housing confidence not so confident

Optimism in the direction of house prices weakened further in the January ASB housing confidence survey. A very slight margin of just 1% net respondents expect house prices to rise over the next year, compared to 12% previously. The survey is a good indicator of activity over the next two to three months, and the survey suggests activity will be very subdued indeed.

RBNZ inflation expectations survey



New Zealand: electronic card transactions and retail trade



The ASB survey follows the REINZ and QVNZ housing market data which recently showed New Zealand's housing market is crumbling under the weight of higher interest rates and reduced net-permanent migration. The pendulum has swung from a seller's market to a buyer's market, and all the street signs are reading 'buyer's beware'.

Electronic card spending weak in January

The relatively new electronic card transaction series, compiled by Statistics NZ, showed a 0.6%m/m fall in core retail sales purchased via electronic card transactions in January. The headline retail spending series showed a small gain of 0.3%m/m. Although the series is still in it's infancy, the correlation with monthly movements in the retail trade survey is strong, and points to very weak spending in January (chart).

Higher interest rates, coupled with rising petrol prices, have hit the consumer purse. The shock of paying more in interest, rent, and petrol is now being compounded by the widespread view that New Zealand's housing market has turned and will, at best, track sideways for the next few years. JPMorgan believes house prices will contract in 2008.

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New Zealand:
Data releases and forecasts

Week of February 25 - 29

Tue
Feb 26
3:00pm

RBNZ inflation expectation
Not seasonally adjusted

	2Q07	3Q07	4Q07	1Q08
(%q/q)	2.6	2.6	2.7	2.8

Wed
Feb 27
10:45am

Building consents
Not seasonally adjusted

	Oct	Nov	Dec	Jan
(%m/m)	4.9	5.0	-20.6	8.0
(%oya)	-12.3	-1.9	-7.7	-0.2

Wed
Feb 27
3:00pm

NBNZ business confidence

	Nov	Dec	Jan	Feb
% balance of respondents	-19.6	-24.9	n/a	-25

Thu
Feb 28
10:45am

Visitor arrivals
Not seasonally adjusted

	Oct	Nov	Dec	Jan
Total (%m/m)	-2.5	2.8	-1.2	__

Net-permanent migration

	Oct	Nov	Dec	Jan
Monthly (000s)	1.6	1.8	-0.1	__
12 month sum (000s)	7.5	6.6	5.5	__

Fri
Feb 29
10:45am

Trade balance
Not seasonally adjusted

	Oct	Nov	Dec	Jan
Exports ($NZ mn)	3369	3373	3677	3700
Imports ($NZ mn)	4142	4001	3644	3800
Trade balance ($NZ mn)	-773	-628	33	-100

Review of past week's data

Credit card spending
Seasonally adjusted

	Nov	Dec	Jan	
(%oya)	9.5	7.6	__	*8.6*

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Global essay

- **Last week's indicator flow remains consistent with a global economy that is bending but not breaking**
- **The Fed is still focused on growth risks, and Bernanke is set to signal this week further rate cuts ahead**
- **Central banks outside the US view growth and inflation risks as more balanced, supported by the indicator flow**
- **Japan posts surprisingly strong exports for January, but manufacturing softening is still in the offing**

There will be blood

The most immediate concern facing the global economy is the fallout from a potential US recession. The resulting sustained contraction in profits and labour income would magnify stress in credit markets that are already impaired. A US recession also would likely spill over to parts of the global financial marketplace that have, as yet, remained relatively unharmed. At present, US growth appears to be stalling, but the economy has shown little sign of a pronounced shift in business and household behaviour that would mark the onset of recession. To be sure, the economy is on a razor's edge, and household purchasing power appears to be getting less relief than expected this quarter from food and energy prices. In addition, continued widening in credit spreads is thwarting the transmission of Fed easing to private sector borrowing rates.

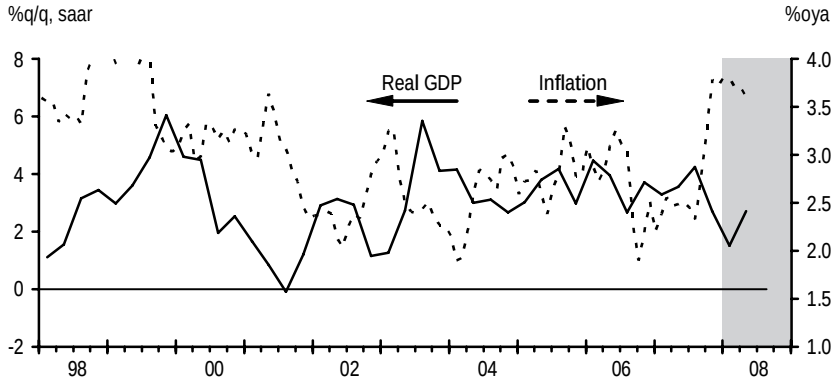
Against this backdrop, the latest news on inflation provides a dose of irony, as it reminds us that medium-term global performance would be best served by sustained subpar US growth. Slowing trends in US productivity and labour supply growth have boosted domestic utilization rates. Combined with the US dollar's decline and an even more impressive rise in utilization rates across the globe, this backdrop continues to lift prices of global commodities and other traded goods. Estimated global headline inflation in January stood at 3.8%oya, the highest level in almost nine years. Excluding food and energy, estimated global inflation last month was 2.2%, a level not seen since 2002.

For the global economy to sustain its impressive run of strong, broad-based growth, inflation pressures need to be reduced. The most desirable path of adjustment would involve a moderation in US domestic demand. If this happens in a manner that maintains the emerging market domestic demand engines and raises US private saving, important steps will have been taken toward a sustained and balanced global expansion. The alternative path, in which global utilization rates remain high and growth is solid, would gradually intensify pressures for a broad shift in central bank policy that woould threaten the life of the global expansion.

In the US, policymakers' aggressive actions to offset recession risks make sense, given the potential for large adverse consequences of a negative feedback loop between growth and credit market stress. Chairman Bernanke is likely to emphasize this risk in this week's testimony, laying the groundwork for additional easing next month. If the US economy is sliding into recession, policy actions that will deliver a large midyear tax rebate and a zero real funds rate will provide a sizable cushion in 2H08, limiting the depth of the slowdown in the US as well as the spillover to the rest of the world.

However, if the US economy skirts recession, policy will add to growth as the drags fade from energy prices increases, declining residential construction, and inventory drawdowns. In this case, the stage will be set for US growth to move above 3% in 2H08, while keeping core inflation well above the top of the Fed's comfort zone.

Global real GDP growth and consumer price inflation



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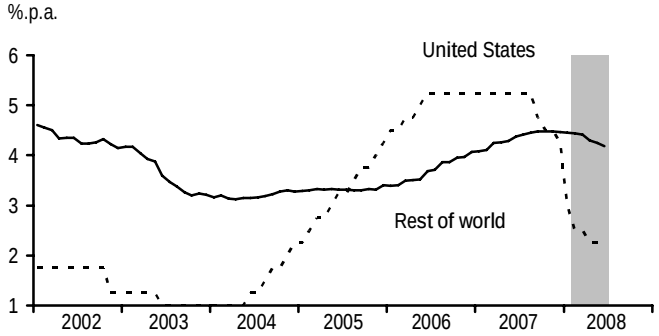
Global policy interest rates



The prospect of such a cyclical bounce—alongside still elevated global inflation, and an accommodative global monetary policy stance—highlights the bimodal nature of the global outlook for 2008. The challenges inherent in a scenario in which the US skirts recession are a reminder to be careful what you wish for.

Central banks challenged by data

Although each of the G-3 economies remains at risk of recession, the indicator flow remains consistent with a global economy that is bending but not breaking. At the same time, recent reports on inflation have surprised on the upside, leading most central banks outside the United States to view risks as more evenly balanced, or even tilted toward inflation. Consequently, barring a significant deterioration in the indicator flow or in financial markets, the extent of monetary easing aside from the Fed probably will be quite limited.

- Even after the FOMC slashed the real federal funds rate target to less than 1%, last week's release of the meeting minutes underscore that growth remains the Fed's dominant concern. The minutes also indicate a growing recognition that rates may need to be kept low for an extended period of time. Notably, the Committee lowered its central-tendency projection for 2008 GDP growth 0.5% point, but raised its forecast for core inflation 0.3% point.

- In the UK, the resilience of retail sales through January, combined with a likely climb in inflation to near 3%oya by midyear, challenges our view that the MPC will ease an additional 50bp to 4.75%. Nonetheless, households face multiple headwinds from sluggish real income growth, tightening non-price terms on credit availability, and levels of interest rates above their recent norms, all against the backdrop of a sagging housing market. The most likely outcome is a marked slowing in spending growth that paves the way for additional rate cuts.

- In the Euro area, the flash PMI survey for February points to GDP growth of 1.5% annualized, alleviating concerns about a sharp slowdown. At the same time, inflation is raising concern. The upcoming January CPI release is likely to confirm headline inflation at 3.2%oya, with core at 2.3%. Also worrisome is a likely acceleration in labour costs, highlighted by last week's steel workers' pay deal in Germany. With most ECB commentary aimed at discouraging market expectations for monetary easing, the risk is that the central bank will not deliver on our forecast for a rate cut in April.

- In Scandinavia, last week's GDP report out of Norway suggests that strong growth, record-high resource use rates, and increasing cost and price pressure all may lead the Norges Bank to tighten, possibly as soon as next month. Downside risks to growth appear more significant in Sweden, whose economy is more open and cannot rely on high oil prices as an extra growth engine. Although the recent rate hike made clear that the Riksbank is still focused on inflation, the minutes of the meeting (out this week) will shed more light on the MPC's thinking. We expect a split vote (possibly 4-2), with some members dissenting for a pause and the MPC showing more concern about growth than the decision alone would imply.

Little relief from the price volatiles

Down the road, the inflation consequences for a global economy that avoids a US recession are greatly amplified by the continued acceleration in energy and food prices, the run-up in the latter perhaps the more pernicious. Conventional wisdom holds that volatility means that energy and food should be discounted when gleaning the underlying thrust of price pressures. However, there is a growing recognition that persistent gains in these high-profile categories of spending have the potential to ignite wage growth or inflation expectations at a time when profit growth is already slowing.

On an over-year-ago basis, monthly energy and food prices combined outpaced core inflation less than 20% of the time during the 1990s expansion but for 80% of this decade's expansion—shades of the 1970s! If anything, price pressures were on the rise entering 2008, with energy and food prices combined rising at the fastest pace in many years.

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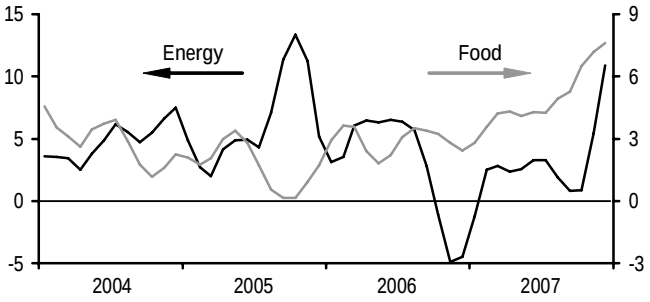
Global consumer energy and food prices

%3m/3m, saar; both scales



Energy prices are increasing more moderately in the current quarter (versus 4Q), reflecting the slower ascent of oil prices. This will reduce, but not eliminate their drag on household purchasing power. However, even if oil prices level off, base effects mean that they will boost the over-year-ago inflation rate throughout this year. In contrast, consumer food prices jumped in January in most parts of the world. Further increases in food prices will likely be fueled by the ongoing surge in global food commodity prices, which statistical evidence suggests can take as long as 12 months to pass through to the consumer level. The upshot is that rising food prices are likely to remain a drag on purchasing power in the coming months, even as they boost monthly and over-year-ago rates of consumer price inflation.

Japan to join global industry slowdown

Exports out of Emerging Asia bounced in January, largely reflecting the typical front-loading of production ahead of the lunar new year in early February. As such, a corresponding dropoff in exports and IP is projected for February. Surprisingly, January exports also surged in Japan, where the holiday effect is usually more muted, suggesting that global demand for its competitively priced, high-end exports may be stronger than anticipated. This certainly is true with respect to the Middle East, where governments are engaged in massive infrastructure building.

This week's reports will provide a closer look at the domestic side of Japan's demand equation. Indicators of consumer spending are expected to be mixed, consistent with a subdued gain in household expenditures again this quarter. The downtrend in the various business surveys also is expected to be maintained. Perhaps of most interest will be the report on January industrial production. Output is forecast to be flat, accompanied by manufacturers' forecasts for a decline in production in February-March. Having increased nearly 6%q/q, saar in 4Q07, an expected IP decline in the current quarter would set the stage for a sharp downshift in real GDP growth after the surprise 3.7% increase last quarter.

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JPMorgan View - Global Markets

Waiting for Godot

- **Markets remain convinced that a US recession is on its way**, if it has not started yet. But conclusive evidence of such a recession is lacking so far. The **US economy has stopped growing, but has not yet started to contract**, which is needed for a recession. To us, it remains a flip of a coin which way we are headed. Given this uncertainty, it is not surprising that bonds and equities have traded in a **noisy range** over the past month. In our base scenario, we will stay in a range for the next few months, until, sometime in 2Q, investors will give up "waiting for Godot," who never comes. By that time, tax rebate checks will arrive to US households, pushing up spending then.

- **Investors generally do not put on new positions** while in waiting mode, **and are more likely to lose patience with old ones**. This explains last week's dramatic curve flattening, as every bond investor has steepeners on. We consider this temporary and stay in steepeners. It also explains why credit has continued to suffer while equities are trying to break out on the upside. Equity investors are heavily long cash, and the return on this cash is slated to fall as central banks ease. Banks and hedge funds, as well as their off-balance-sheet vehicles, remain burdened by uncomfortable longs and unsold inventory, thus putting further pressure on spreads. Spread widening is not attracting sufficient buyers, though, and we thus stay bearish on credit, and underweight against equities.

- We know asset allocators are long **EM** assets, and it's good to see they are not excessively nervous, as EM equities are moving in line with developed markets while EM currencies in a range. We are medium-term bullish on EM equities, fx, and credit (but not local bonds given inflation risks there), as fundamentals are supportive and EM is far removed from the turmoil in US credit. However, the presence of the strategic EM overweight is keeping us for the moment with only small longs in EM, focused on EM equities.

Fixed income

- **Bonds declined last week**, largely as short-maturity yields backed up, itself the result of profit-taking on steepeners. **We stay long the short end and in steepeners in Europe and the US.**

- The short end of the **US** curve prices in that fed funds will bottom at 2.25%, which matches our forecasts. But with risk still biased on the downside, and a recession likely pushing this rate to 1.5%, we see value at the short end in the US.

10-yr Government bond yields

	Current	Mar 08	Jun 08	Sep 08	Dec 08
United States	3.74	3.80	4.00	4.15	4.20
Euro area	4.01	3.85	3.70	3.70	3.60
United Kingdom	4.68	4.55	4.35	4.50	4.65
Japan	1.44	1.30	1.45	1.60	1.85

Equities

	Current	YTD Return (local currency)
S&P	1330	-8.3%
Topix	1321	-9.5%
FTSE 100	5889	-7.8%
MSCI Eurozone	212	-12.7%
MSCI Europe	1372	-10.9%

Credit markets

	Current	Jun 08	Dec 08
US high grade (bp over UST)	227	175	
US high grade (bp over swaps)	143	100	
Euro HG corp (bp over swaps)	87		65
USD high yield (bp vs. UST)	737	800	650
EMBIG (bp vs. UST)	294	250	200

Foreign exchange

	Current	Mar 08	Jun 08	Sep 08	Dec 08
EUR/USD	1.48	1.54	1.55	1.55	1.54
USD/JPY	107	98	101	101	103
GBP/USD	1.97	2.03	2.04	2.05	2.05

Commodities

		Quarterly Average			
	Current	Mar 08	Jun 08	Sep 08	Dec 08
WTI oil $/bbl	99.2	86.0	72.0	72.0	76.0
Gold ($/oz)	945	920	920	915	900
Copper($/m ton)	8487	8000	7300	6500	6000
Corn ($/Bu)	5.36	4.90	4.70	4.30	4.80

Source: JPMorgan, Bloomberg, Datastream

Be long. Rising duration supply should keep upward pressure on 5s and 10s, and we thus stay in steepeners, a widely held position. We similarly hold longs and steepeners in Europe.

- Last year's run on SIVs and conduits has become this year's run on the short-dated **US municipal debt and money market**. The crisis is purely a liquidity one, so far, but is again leading to a closure of the money market, forcing issuers to switch to long-dated, fixed rate issues. Thus further supports curve steepening, but also raises the risk of banks having to acquire these instruments.

Equities

- Equities remain in a noisy range on mixed economic and earnings data, and are set to stay this way for several more months. We are long against both credit and bonds, as equity investors appear long cash while specs seem balanced.

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Credit, in contrast, suffers from an overhang of unwanted exposures while bond investors are long.

- **EM** equities are largely moving in line with developed markets, having outperformed them by 1% ytd. We stay long EM vs developed markets on strong commodity prices and supportive EM economic news.

- Across **sectors**, we favour **defensive plays**, underweight-ing consumer-exposed sectors such as consumer discretionary against defensive sectors such as healthcare. **Financials and IT are the worst performing sectors ytd.** We project these sectors to outperform into year end on value, assuming that even if a US recession takes place, it will be short-lived and contained within the US. Near term, though, these sectors face headwinds. Financials are heavily exposed to worsening credit market problems. The IT sector, especially in EM Asia, is highly levered to the weakening global growth cycle. Indeed, Asian tech exports slowed sharply in 4Q, and are set to slow further in 1Q. In addition, expectations of cuts in tech spending by banks and rising costs for materials are weighing negatively on the sector.

- Growth beat value again last week and is now outperforming ytd. Stay **long growth vs value globally.** Historical evidence shows that growth tends to outperform value into recessions. A reversal of this trend takes place in the middle of a recession or immediately after. This means that the growth vs value outperformance that started last May has at least a few more months to run, with recession risks remaining elevated.

Credit

- **Credit spreads kept widening last week,** led again by attempts at unwinding of synthetic structures. The CDS-bond basis keeps rising, reaching 9bp in US High Grade versus -40bp one month ago. Further position unwinding should continue to put more pressure on the CDS-bond basis near term, CDS curves are set to slowly steepen as 7 and 10-year structures are unwound.

- The unwinding of credit structures is driven by both mark-to-market losses and rating downgrades, but the latter is likely more important. Indeed, unwinds of transactions did not increase noticeably until a new rating methodology was proposed earlier this month. The risk of further downgrades has risen considerably and we thus see upward pressure in credit spreads near term. **Credit is extremely cheap** but in the absence of positive news and liquidity having dried up, value investors are reluctant to jump in.

- In **high yield**, the primary market remains practically closed as the unsold inventory of loans and bonds, related to previous LBO deals, deters prospective buyers. With spreads close to 700bp, high-yield loans are very cheap vs bonds. Without any demand for high yield bonds, we believe that this value discrepancy will be resolved by wider bond spreads in the next few months. Stay bearish, favouring loans vs bonds and BBs over CCCs within bonds.

Foreign exchange

- The dollar fell against all currencies except for CAD on another round of poor macro data. We had been expecting **EUR/USD** to hold a range (1.44 - 1.49) near term given the weakness of European data as well, but the PMI reports suggest somewhat more resilience in Europe. With EUR longs negligible, EUR/USD could break to new highs this quarter absent a rebound in US data.

- **Peripheral markets** continue to demonstrate more momentum than the G-3 pairs since their rates are higher and policy stances firmer: most are tightening. Combined with supply constraints pushing commodity prices higher, this means that AUD, NZD, and NOK will likely be the strongest currencies this quarter. We are long AUD vs USD and CAD, and long NOK vs CAD.

- **Emerging market currencies** are exhibiting notable divergences, with Asia rallying while CEEMEA weakens. The moves are mostly in line with the regions' respective balance of payments positions, but the resilience of Asian currencies is still surprising in a weak equity market environment. Throughout EM we prefer cross-rate trades (long TRY/ZAR, long BRL/MXN, long SGD/KRW) to outright longs in EM.

Commodities

- **Base and precious metals** continue to soar, aided by a weak dollar, supply disruptions (precious metals) and inventory drawdowns (copper). The decoupling themes may continue to support both sectors near term but, given doubts around that view, precious metals are still the better trade for the first half of the year. **Crude** made a new all-time high this week above $100/bbl, but we see its rise as the least credible within the commodity complex. Unlike metals, which are experiencing supply disruptions or inventory draws, crude stock positions have been improving for the past several weeks. We expect lower prices this spring, but the weak dollar environment is an impediment to a quick fall.

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Markets - Australia and New Zealand

- **RBA considered hiking interest rates 50bp in February**
- **Rising labour costs a concern for the RBA**
- **RBNZ inflation expectations survey out Tuesday**

Market commentary

Australia

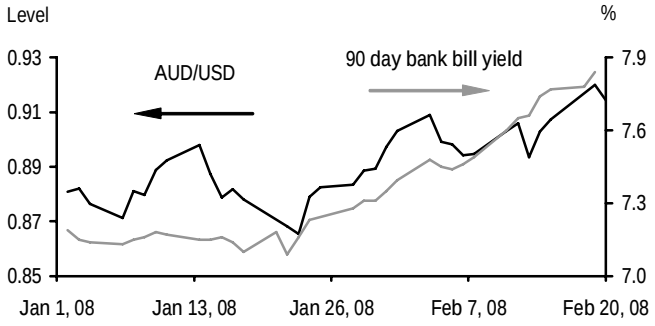
Last week's minutes from the RBA's February monetary policy meeting showed that RBA officials considered hiking interest rates 50bp at their last meeting. On February 5, however, a 25bp hike was judged "more persuasive" by the RBA given several domestic banks had recently lifted their standard variable loan rates in the absence of a rise in the official cash rate. The fact that Board members even debated a 50bp move led market pricing to suggest a 95% chance of a 25bp rate hike next month, up from 84% following the bank's hawkish Statement on Monetary Policy a week earlier.

The RBA minutes also showed that the Board decided that further tightening could be implemented in March, or thereafter, if policy was judged not restrictive enough. The current tightening cycle clearly is not yet over. Our forecast is that the RBA will raise the cash rate 25bp in March and then again in May, just after the release of the 1Q CPI data, which will show another elevated inflation reading. The RBA forecasts the underlying trend in inflation is now around 3.5%, and remains concerned that rising inflation might feed back into domestic wage and price expectations.

Regarding wage cost pressures, the minutes also highlighted the tight labour market, but noted that wage growth to date had remained largely contained. The RBA pointed out, though, that average earnings from the national accounts had showed a significant pick up in wage growth. The minutes were followed by economic data midweek showing that wage growth picked up in 4Q, with the labour price index rising 1.1%q/q compared to 1.0% in the previous quarter.

As the likelihood of a March rate hike increased, the AUD headed north last week. After starting the week at just over 90 US cents, the aussie rallied to a high of nearly 92.40 US cents midweek, although shed some of its gains to close the week just under 92 US cents. The local equity market remained volatile in the midst of the reporting season, and finished slightly lower on the week. The Aussie 3s 10s curve steep-

Prospective March rate hike drives AUD and yields north



ened, meanwhile, with the longer end continuing to follow trends offshore.

New Zealand

RBNZ inflation expectations are on the rise. The RBNZ inflation expectations survey, out this Tuesday, should gather some interest in the market. Inflation expectations is a major input in the RBNZ's inflation model, and expectations are likely to have risen in 1Q. Inflation expectations tend to track oil and food prices, both of which have increased substantially in recent months. Rising inflation expectations will worsen the inflation outlook, and keep the possibility of an interest rate cut off the table (chart).

That said, whilst the inflation trajectory will keep RBNZ officials on guard, the chances of a further rate rise in this cycle are diminishing by the day. New Zealand's housing market has turned south harder and faster than RBNZ forecasts, and an unfortunate drought in New Zealand's major dairy producing regions is taking a slice out of growth in export volumes. We expect the RBNZ to downwardly revise its housing market forecasts in the March quarter monetary policy statement to reflect a slight decline in house prices—somewhere in the order of -5% in 2008—and a minor cut in export volumes growth.

Last week's housing confidence survey, and electronic card transactions series showed consumers are worried about the outlook for housing, and are being hit hard by rising interest rates and surging petrol prices. In this environment, consumption growth will ease and housing market activity will continue south.

The market basically tracked sideways last week, despite the

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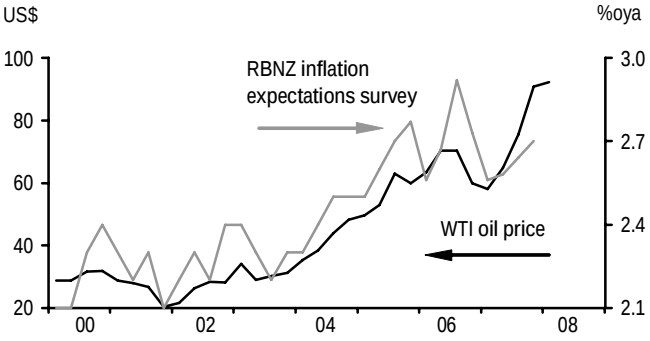
weakening local data, and our short Kiwi 3 month into 2 year strangle is comfortably in its range and remains on track. The NZD also slid sideways over the week, and followed movements in the AUD. AUD/NZD has traded in a narrow 75pt range over the week, between 1.1400 to 1.1475.

We see the AUD/NZD rising back towards 1.20 on narrowing interest rate differentials—the RBA is likely to raise rates twice more in coming months to 7.5%, while the RBNZ is likely to keep the official cash rate unchanged at 8.25%.

Trade recommendations

- Hold long Aussie Mar08 bank bills vs. short Jun08 bills in futures. Established at 1bp two weeks ago (with target of 10 and a stop loss at -4), the position has traded to 6bp, for a 7bp gain.
- Hold short Kiwi 3 month into 2 year strangle using strikes 8.75% to 8.55%. Pick up 44pts with breakeven points at 8.99% and 8.31%. The position is back to trading in the middle of the range.

New Zealand: WTI oil price and inflation expectations



AUD and NZD Commentary

- **AUD and NZD strengthen against the dollar on commodities outperformance despite wobbly carry environment**
- **RBA minutes show a more hawkish policy stance; further tightening expected from the RBA**
- **Technicals: AUD and NZD reassert interim rallies vs USD**

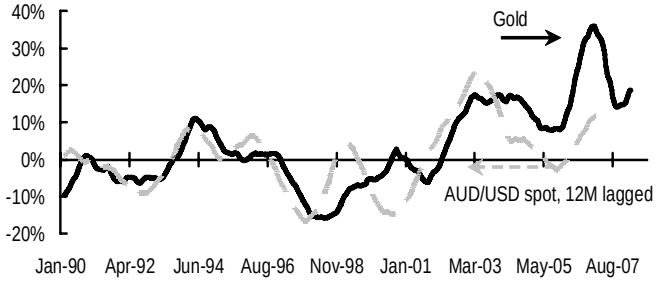
Strategy comments

- The Antipodeans rallied about 2% against USD, partly reflecting the resumption of the broad dollar bear trend and outperformance in the commodities block. The resilience of the two currencies is particularly notable within a global backdrop that is hardly carry-friendly, given equities remain fragile, US data shows continues to disappoint, and volatility remains elevated. We believe, however, that AUD and to a lesser degree NZD outperformance is supported by a combination of positive drivers that are likely to persist near term.
- The big news in Australia last week were the RBA's minutes. Key for market perceptions was a passage in which the RBA acknowledged policymakers debated the necessity of an immediate hike of 50bps at the Feb. 5 meeting. Their main concern appears to be the signs of higher inflation expectations, which could raise "the cost of reducing inflation over time". The Bank's rhetoric, including the words of Assistant Governor Edey, leaves little room to doubt a 25bps hike is forthcoming. The effect of such outcome on AUD will likely be subdued given economists almost unanimously expect further tightening. JPMorgan expects a 25bps hike at both the March and May meeting to take policy rates to 7.5%.
- In NZ the data flow was light last week, with kiwi trading mainly in tandem with AUD and commodities. The first important data point over the next two weeks will be inflation expectations on Feb. 26. Given the role of expectations as a major input into the RBNZ's monetary policy decision, this release will help shaping expectations ahead of the Bank's March 5 MPM. While somewhat secondary, building permits (also out on Feb. 26) will be watched closely as weakness in the housing sector remains a key vulnerability in NZ's economy. While the macroeconomic outlook for Australia remains a bullish factor for the currency, NZD would come under pressure should construction deteriorate sufficiently as to impact the risk-perceptions and policy stance of the RBNZ.
- The RBA's hawkish posture makes Australia the most compelling decoupling story among G10 economies. Furthermore, external support from rallying metals and bulk commodity prices, coupled with light speculative positions, should also help AUD outperform against G10 FX more broadly. In particular, the rally in gold signals further AUD strength is likely based on a 0.70 historical correlation between the two series. We therefore remain long AUD/USD and added to our AUD exposure through a long AUD/CAD position.

Gold signals further AUD strength

Gold and AUD/USD, yoy %chg in the 12-month moving average

AUD/USD is lagged by 12 months



Technical analysis

- A bullish week for AUD/USD with the breakout above the key 0.91 resistance zone setting the stage for a continuation of the interim rally. While the advance has developed in an impulsive manner and suggests further upside, the action from here will likely be more of a grind higher. For the very short term setup, the 0.9100/.9110 area will act as key support and maintain the upside bias. Expect a test of initial resistance at 0.9300/.9320 area followed by the critical 0.9400 November peak, which should be where prices struggle.
- For NZD/USD, the interim rally phase continues to develop and should allow for a breakout through the important 0.8110 July high. Note Friday's advance took on a more impulsive bias, which seems consistent with additional NZD strength. New highs would seek 0.8210/.8270 levels. Support at 0.8020 and 0.7955 will now maintain the more immediate upside bias.

NZD/USD - Daily technical chart

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Global Economic Outlook Summary

	Real GDP			Real GDP							Consumer prices			
	% over a year ago			% over previous period, saar							% over a year ago			
	2006	2007	2008	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	4Q07	2Q08	4Q08	2Q09
The Americas														
United States	2.9	2.2	1.9	4.9	0.6	0.0	2.0	3.5	2.5	3.5	4.0	**3.5 ↑**	**2.7 ↑**	2.3
Canada	2.8	2.5	1.3	2.9	0.8	-1.0	1.5	2.8	2.8	3.0	2.4	1.0	1.6	1.7
Latin America	5.3	**5.2 ↑**	4.3	**7.0 ↑**	**5.8 ↑**	**3.1 ↓**	3.4	**4.0 ↑**	**4.5 ↓**	4.5	5.6	**6.3 ↑**	**6.1 ↑**	5.9
Argentina	8.5	8.7	6.5	11.8	10.4	3.2	4.9	4.1	4.1	4.1	8.5	8.6	9.7	11.0
Brazil	3.8	5.4	4.9	6.9	5.3	4.9	4.3	3.7	4.2	4.1	4.2	4.2	4.2	4.3
Chile	4.0	5.2	4.0	-2.5	8.0	5.0	3.0	3.0	5.0	5.0	7.2	8.2	4.8	3.1
Colombia	6.8	6.8	5.5	6.9	5.0	5.0	5.5	6.5	6.5	4.5	5.4	**5.5 ↑**	**5.0 ↑**	4.0
Ecuador	3.9	2.0	2.5	4.4	5.0	2.0	1.5	1.0	1.0	2.5	2.8	4.1	3.3	3.3
Mexico	4.8	**3.3 ↑**	2.7	**5.3 ↓**	**3.0 ↑**	1.0	2.0	4.1	4.9	4.9	3.8	4.7	4.1	3.3
Peru	7.6	**9.0 ↑**	**7.5 ↑**	15.9	**19.0 ↑**	**2.0 ↓**	**4.0 ↑**	**5.0 ↑**	**4.5 ↓**	6.5	3.5	**3.9 ↑**	**2.7 ↑**	**2.5 ↑**
Venezuela	10.3	**8.4 ↑**	6.0	**14.2 ↑**	**11.0 ↑**	5.0	4.0	4.0	3.5	4.0	20.2	24.8	26.6	29.3
Asia/Pacific														
Japan	2.4	2.1	1.7	1.3	3.7	0.5	2.0	2.3	2.3	2.4	0.5	0.8	0.7	0.5
Australia	2.8	3.8	3.5	4.1	3.1	3.2	4.4	2.5	4.1	3.6	3.0	2.9	2.4	2.6
New Zealand	1.5	3.0	2.5	2.1	2.9	2.5	2.7	1.8	2.2	2.9	3.2	3.1	2.9	2.8
Asia ex. Japan	8.5	8.5	7.7	**8.1 ↓**	**6.6 ↑**	**7.4 ↓**	7.7	**7.9 ↑**	**8.1 ↓**	8.0	5.3	5.1	3.8	4.1
China	11.1	11.4	10.5	8.9	9.1	10.8	11.2	10.4	10.4	10.8	6.6	5.6	3.5	4.1
Hong Kong	6.8	6.0	5.3	7.0	5.0	4.0	5.2	5.5	5.5	5.2	3.4	3.4	2.7	3.8
India	9.6	8.7	7.5	8.4	5.3	8.2	7.0	7.5	8.2	8.2	5.5	6.3	5.9	5.2
Indonesia	5.5	6.3	6.2	7.8	6.9	6.0	6.0	6.0	6.0	5.0	6.7	6.9	7.4	7.8
Korea	5.0	4.9	4.8	5.4	6.3	3.0	4.0	5.5	6.0	5.0	3.4	3.4	3.1	3.2
Malaysia	5.9	6.0	5.3	9.7	3.2	4.1	5.7	5.7	6.6	6.1	2.2	3.3	3.8	3.3
Philippines	5.4	7.1	6.1	4.0	7.4	6.0	5.0	5.5	6.0	5.8	3.3	3.2	2.4	2.4
Singapore	8.2	7.7	4.6	5.1	-4.8	6.6	4.1	8.7	9.5	5.7	4.1	5.1	2.8	2.8
Taiwan	4.9	**5.7 ↑**	**4.0 ↓**	**12.0 ↓**	**2.6 ↑**	**0.8 ↓**	**2.5 ↓**	**4.5 ↑**	**5.0 ↓**	**4.8 ↓**	**4.5 ↑**	4.0	1.7	2.4
Thailand	5.1	4.2	5.1	5.8	4.0	6.0	6.0	6.0	5.0	4.5	2.9	4.4	3.8	3.0
Africa														
South Africa	5.4	5.0	3.7	4.7	3.6	2.8	3.8	4.1	4.0	3.7	8.4	**8.5 ↑**	**6.5 ↑**	**5.3 ↑**
Europe														
Euro area	2.9	2.7	1.7	3.1	1.7	1.2	1.2	2.3	2.3	2.5	2.9	2.7	2.3	2.3
Germany	3.1	2.6	1.6	2.7	1.1	1.3	1.3	2.3	2.3	2.5	3.1	2.0	1.4	1.5
France	2.2	1.9	1.8	3.2	1.4	1.5	1.3	2.3	2.3	2.3	2.5	2.4	1.8	2.0
Italy	1.9	1.7	0.7	1.7	-0.8	0.5	0.5	2.0	2.0	2.3	2.6	2.6	2.2	2.3
Norway	**4.8 ↑**	**6.0 ↑**	**3.9 ↑**	**7.9 ↑**	**3.8 ↑**	3.0	2.5	3.0	3.0	3.5	1.4	5.0	3.4	2.2
Sweden	4.4	2.8	2.4	2.4	2.8	2.0	2.0	3.0	3.0	3.5	3.1	3.6	3.0	2.5
Switzerland	3.2	2.8	1.8	3.3	2.0	1.3	1.1	1.8	1.8	2.0	1.7	1.6	1.5	1.3
United Kingdom	2.9	3.1	2.0	2.7	2.4	1.2	1.6	2.0	2.3	2.5	2.1	2.4	2.7	2.1
Emerging Europe[1]	6.6	6.6	5.7	6.4	10.2	0.4	7.5	5.7	8.4	1.2	8.1	8.6	7.0	5.8
Bulgaria	6.1	6.1	5.2	...	...	...	...	...	...	...	...	...	...	...
Czech Republic	6.4	6.6	5.0	5.8	7.8	3.5	4.5	3.5	4.5	5.5	4.8	7.1	5.5	3.0
Hungary	3.9	1.3	2.0	0.8	0.4	2.8	2.8	3.0	3.0	3.0	7.1	5.9	4.3	3.7
Poland	6.2	6.5	5.5	4.9	8.2	4.5	4.8	5.3	5.5	5.8	3.5	4.1	3.8	3.3
Slovak Republic	8.5	10.3	7.0	9.2	17.9	-2.0	6.0	7.0	7.0	4.0	3.3	4.3	3.6	4.0
Romania	7.7	6.0	5.6	...	...	...	...	...	...	...	6.7	6.5	5.5	5.3
Russia	7.4	8.1	6.8	7.4	13.0	-2.5	10.5	6.5	12.0	-2.5	11.5	12.6	10.1	8.8
Turkey	6.1	5.0	5.0	...	...	...	...	...	...	...	8.2	7.4	6.2	4.1
Global	3.7	3.4	2.7	4.4	**2.8 ↑**	1.5	**2.7 ↓**	3.5	3.4	3.5	3.5	**3.4 ↑**	**2.8 ↑**	2.6
Developed markets	2.8	2.5	1.9	3.6	1.6	0.6	1.8	2.8	2.4	2.9	2.9	**2.7 ↑**	**2.2 ↑**	2.0
Emerging markets	7.0	7.0	6.1	7.5	**7.0 ↑**	**5.0 ↓**	6.5	**6.5 ↑**	7.2	5.9	5.9	**6.1 ↑**	5.0	4.8

Note: For some emerging economies, 2006-2008 quarterly forecasts are not available and/or seasonally adjusted GDP data are estimated by JPMorgan.
Bold denotes changes from last edition of *Global Data Watch*, with arrows showing the direction of changes.

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Global Central Bank Watch

	Official interest rate	Current	Change from Jun 04 (bp)	Last change	Forecast next change	Mar 08	Jun 08	Sep 08	Dec 08	Mar 09
Global	GDP-weighted average	3.98	145			3.81	3.57	3.56	3.61	3.67
excluding US	GDP-weighted average	4.44	130			4.43	4.19	4.19	4.25	4.35
Developed	GDP-weighted average	3.21	160			3.00	2.70	2.70	2.74	2.83
Emerging	GDP-weighted average	7.11	81			7.10	7.11	7.09	7.14	7.12
The Americas	GDP-weighted average	3.72	145			3.27	3.02	3.00	2.99	3.00
United States	Federal funds rate	3.00	175	30 Jan 08 (-50bp)	18 Mar 08 (-50bp)	2.50	2.25	2.25	2.25	2.25
Canada	Overnight funding rate	4.00	200	22 Jan 08 (-25bp)	4 Mar 08 (-50bp)	3.50	2.75	2.75	2.75	3.00
Brazil	SELIC overnight rate	11.25	-475	5 Sep 07 (-25bp)	2Q 09 (-25bp)	11.25	11.25	11.25	11.25	11.25
Mexico	Repo rate	7.50	100	26 Oct 07 (+25bp)	15 Aug 08 (-25bp)	7.50	7.50	7.25	7.00	7.00
Chile	Discount rate	6.25	450	10 Jan 08 (+25bp)	10 Jul 08 (-25bp)	6.25	6.25	6.00	5.75	5.75
Colombia	Repo rate	**9.75**	300	**22 Feb 08 (+25bp)**	1Q 09 (-25bp)	**9.75**	**9.75**	**9.75**	**9.75**	**9.50**
Peru	Reference rate	5.25	275	10 Jan 08 (+25bp)	on hold	5.25	5.25	5.25	5.25	5.25
Europe/Africa	GDP-weighted average	4.53	166			4.54	4.10	4.10	4.11	4.28
Euro area	Refi rate	4.00	200	6 Jun 07 (+25bp)	10 Apr 08 (-25bp)	4.00	3.50	3.50	3.50	3.75
United Kingdom	Repo rate	5.25	75	7 Feb 08 (-25bp)	10 Apr 08 (-25bp)	5.25	4.75	4.75	4.75	4.75
Sweden	Repo rate	4.25	225	13 Feb 08 (+25bp)	17 Dec 08 (+25bp)	4.25	4.25	4.25	4.50	4.75
Norway	Deposit rate	5.25	350	12 Dec 07 (+25bp)	3Q 08 (+25bp)	5.25	5.25	5.50	5.75	5.75
Czech Republic	2-week repo rate	3.75	150	7 Feb 08 (+25bp)	26 Mar 08 (+25bp)	4.00	4.00	4.00	3.75	3.50
Hungary	2-week deposit rate	7.50	-400	24 Sep 07 (-25bp)	**25 Feb 08 (+25bp)**	**8.00**	**8.00**	**8.00**	**8.00**	**7.75**
Poland	7-day intervention rate	5.25	0	30 Jan 08 (+25bp)	**27 Feb 08 (+25bp)**	**5.50**	**5.50**	**5.75**	**6.00**	**6.00**
Russia	1-week deposit rate	3.50	250	4 Feb 08 (+25bp)	1Q 09 (+25bp)	3.50	3.50	3.50	3.50	3.75
Slovak Republic	2-week repo rate	4.25	-75	27 Apr 07 (-25bp)	2Q 08 (-75bp)	4.25	3.50	3.50	3.50	3.75
South Africa	Repo rate	11.00	300	6 Dec 07 (+50bp)	**Feb 09 (-50bp)**	**11.00**	**11.00**	**11.00**	**11.00**	**10.50**
Switzerland	3-month Swiss Libor	2.75	225	13 Sep 07 (+25bp)	Jun 08 (-25bp)	2.75	2.50	2.50	2.50	2.50
Turkey	Overnight borrowing rate	15.25	-675	14 Feb 08 (-25bp)	19 Mar 08 (-25bp)	15.00	14.00	13.50	13.50	13.00
Asia/Pacific	GDP-weighted average	3.61	114			3.61	3.66	3.68	3.85	3.86
Australia	Cash rate	7.00	175	5 Feb 08 (+25bp)	4 Mar 08 (+25bp)	7.25	7.50	7.50	7.50	7.50
New Zealand	Cash rate	8.25	250	26 July 07 (+25bp)	1Q 09 (-25bp)	8.25	8.25	8.25	8.25	8.00
Japan	Overnight call rate	0.50	50	21 Feb 07 (+25bp)	4Q 08 (+25bp)	0.50	0.50	0.50	0.75	0.75
Hong Kong	Discount window base	4.50	200	23 Jan 08 (-75bp)	19 Mar 08 (-50bp)	4.00	3.75	3.75	3.75	3.75
China	1-year working capital	7.47	216	20 Dec 07 (+18bp)	2Q 08 (+27bp)	7.47	7.74	7.92	8.19	8.19
Korea	Overnight call rate	5.00	125	9 Aug 07 (+25bp)	1Q 09 (+25bp)	5.00	5.00	5.00	5.00	5.25
Indonesia	BI rate	8.00	66	6 Dec 07 (-25bp)	3 Apr 08 (-25bp)	8.00	7.75	7.75	7.75	7.75
India	Repo rate	7.75	175	30 Mar 07 (+25bp)	Jul 08 (-25bp)	7.75	7.75	7.50	7.50	7.25
Malaysia	Overnight policy rate	3.50	80	26 Apr 06 (+25bp)	on hold	3.50	3.50	3.50	3.50	3.50
Philippines	Reverse repo rate	5.00	-175	31 Jan 08 (-25bp)	on hold	5.00	5.00	5.00	5.00	5.00
Thailand	1-day repo rate	3.25	200	18 July 07 (-25bp)	27 Feb 08 (-25bp)	3.00	2.75	2.75	2.75	2.75
Taiwan	Official discount rate	3.375	200	20 Dec 07 (+12.5bp)	1Q 09 (+12.5bp)	3.375	3.375	3.375	3.375	3.50

Bold denotes move this week and forecast changes

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Forecasts - Australia and New Zealand

Australia: economic projections *percentage change over previous period, seasonally adjusted annual rates, un*

				2007			2008				2009			
	2007	2008	2009	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Chain volume GDP	3.8	3.5	3.2	2.8	4.1	3.1	3.2	4.4	2.5	4.1	3.6	2.8	3.1	0.6
Private consumption	4.0	3.5	2.6	1.5	5.0	3.2	4.1	3.2	2.8	2.8	2.4	2.8	2.0	1.6
Construction investment	10.2	3.0	1.3	4.3	5.3	1.9	2.8	4.2	0.5	3.1	2.1	-1.2	0.4	1.4
Equipment investment	7.1	2.4	-2.3	20.7	-8.9	4.2	2.1	8.6	-4.1	0.0	-2.1	-4.1	-8.1	0.0
Public investment	4.0	6.8	6.2	90.3	-8.7	4.2	4.7	5.2	5.4	5.8	6.2	6.6	7.0	7.5
Government consumption	2.7	3.4	2.8	0.7	4.2	2.2	4.4	3.7	3.3	2.9	3.5	2.2	1.8	2.2
Exports of goods & services	4.0	5.8	7.6	2.5	9.4	4.1	6.1	6.1	4.1	8.2	8.2	8.2	10.4	4.1
Imports of goods & services	10.0	4.8	2.6	5.8	9.4	5.1	6.1	2.0	1.6	3.2	3.2	2.4	1.8	3.2
Contributions to GDP growth:														
Domestic final sales	4.6	3.7	2.3	5.6	3.1	4.1	3.9	4.1	2.2	2.9	2.4	1.8	1.2	1.8
Inventories	0.7	-0.3	0.0	-1.8	1.3	-0.6	-0.5	-0.4	-0.1	0.3	0.3	-0.2	0.2	-1.3
Net trade	-1.4	0.1	1.0	-0.8	-0.3	-0.4	-0.2	0.8	0.5	0.9	0.9	1.1	1.7	0.1
GDP deflator (%oya)	3.7	2.8	2.6	4.4	3.1	2.9	2.9	2.9	2.9	2.7	2.6	2.6	2.6	2.5
Consumer prices (%oya)	2.3	3.8	2.9	2.1	1.9	3.0	4.1	3.7	3.8	3.5	3.1	3.0	2.8	2.8
Producer prices (%oya)	2.1	2.6	2.5	1.5	0.8	2.5	3.5	1.7	2.7	2.6	2.5	2.5	2.5	2.5
Trade balance (A$ bil, sa)	-19.2	-22.3	-14.6	-4.4	-5.0	-5.9	-6.1	-5.8	-5.6	-4.8	-4.5	-3.9	-3.2	-3.1
Current account (A$ bil, sa)	-65.4	-73.3	-68.6	-15.6	-15.6	-18.9	-18.6	-18.8	-18.6	-17.3	-18.0	-17.9	-16.7	-16.1
as % of GDP	-6.0	-6.4	-5.6	-5.8	-5.7	-6.8	-6.6	-6.6	-6.4	-5.9	-6.0	-5.9	-5.4	-5.2
3m eurodeposit rate (%)*	6.0	7.3	6.8	5.8	7.1	7.2	7.3	7.3	7.3	7.1	6.9	6.8	6.8	6.7
10-year bond yield (%)*	5.6	6.4	6.3	5.6	5.7	6.4	6.5	6.5	6.5	6.3	6.3	6.3	6.3	6.3
US$/A$*	0.75	0.90	0.84	0.74	0.77	0.88	0.88	0.90	0.91	0.90	0.88	0.85	0.82	0.79
Commonwealth budget (FY, A$ bil)	13.6	8.5	6.0											
as % of GDP	1.3	0.7	0.5											
Unemployment rate	4.3	4.7	5.5	4.3	4.3	4.3	4.5	4.6	4.8	5.0	5.3	5.4	5.6	5.7
Industrial production	2.8	0.7	0.8	1.7	-0.5	-1.0	0.0	1.0	3.0	4.0	-1.0	-2.0	-3.0	0.0

*All financial variables are period averages

New Zealand: economic projections *percentage change over previous period, seasonally adjusted annual rates, unless stated*

				2007			2008				2009			
	2007	2008	2009	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Real GDP (1995-96 prices)	3.0	2.5	2.8	3.3	2.1	2.9	2.5	2.7	1.8	2.2	2.9	3.5	3.3	2.6
Private consumption	4.1	1.3	1.6	1.8	1.3	1.2	1.1	1.2	1.4	1.5	1.6	1.8	1.9	2.0
Fixed Investment	3.1	0.4	2.3	-2.9	-0.9	1.6	0.6	0.4	0.5	1.7	2.9	2.9	3.2	4.0
Residential construction	4.9	-0.8	-1.5	14.8	7.9	1.6	-3.2	-4.0	-8.0	-4.0	-1.6	1.6	3.2	4.0
Other fixed investment	2.6	0.7	3.3	-6.9	-3	1.6	1.6	1.6	2.8	3.2	4.0	3.2	3.2	4.0
Inventory change (NZ$ bil, saar)	0.9	0.4	0.5	0.4	0.3	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Government spending	4.1	5.9	4.0	4.2	8.8	4.4	5.6	6.9	5.8	4.7	2.4	4.4	2.9	2.4
Exports of goods & services	2.5	3.6	4.4	-3.2	-2.3	8.0	5.0	3.6	4.0	4.2	4.5	4.8	5.0	4.5
Imports of goods & services	7.5	2.7	3.0	10.8	0.9	2.2	2.4	2.2	3.0	3.0	3.5	3.0	2.5	3.0
Contributions to GDP growth:														
Domestic final sales	4.3	2.8	2.4	3.5	4.4	4.1	1.9	2.1	2.1	2.3	2.3	2.9	2.5	2.3
Inventories	0.6	-0.4	0.1	4.7	-1.1	-2.7	0.0	0.2	-0.5	-0.2	0.5	0.2	0.1	0.0
Net trade	-1.9	0.1	0.3	-4.8	-1.1	1.6	0.7	0.3	0.2	0.2	0.1	0.4	0.7	0.3
GDP deflator (%oya)	3.7	3.3	2.8	4.1	3.8	3.8	3.8	3.2	3.0	3.0	2.9	2.8	2.7	2.7
Consumer prices	2.4	3.2	2.7	4.0	2.0	4.8	3.0	2.7	3.1	2.8	2.7	2.6	2.7	2.5
%oya	2.4	3.2	2.7	2.0	1.8	3.2	3.4	3.1	3.4	2.9	2.8	2.8	2.7	2.6
Trade balance (NZ$ bil, sa)	-3.7	-5.3	-4.1	-0.8	-0.8	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3	-1.1	-1.0	-0.8
Current account (NZ$ bil, sa)	-14.5	-14.8	-13.5	-3.5	-3.6	-3.8	-3.7	-3.7	-3.6	-3.7	-3.7	-3.5	-3.3	-3.0
as % of GDP	-8.5	-8.2	-7.1	-8.3	-8.5	-8.7	-8.4	-8.2	-8.1	-8.2	-8.0	-7.5	-6.8	-6.1
Yield on 90-day bank bill (%)*	8.4	8.4	7.8	8.2	8.7	8.8	8.4	8.4	8.4	8.4	8.0	7.9	7.6	7.5
10-year bond yield (%)*	6.3	6.6	7.0	6.4	6.4	6.4	6.5	6.6	6.7	6.8	7.0	7.1	7.0	7.0
US$/NZ$*	0.74	0.77	0.68	0.74	0.74	0.76	0.78	0.77	0.77	0.76	0.70	0.66	0.67	0.68
Commonwealth budget (NZ$ bil)	6.4	5.3	5.0											
as % of GDP	3.8	2.9	2.6											
Unemployment rate	3.6	4.0	4.5	3.6	3.5	3.7	3.8	3.9	4.1	4.2	4.3	4.5	4.6	4.7

*All financial variables are period averages

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Australia and New Zealand economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
25 Feb	26 Feb New Zealand: RBNZ inflation expectation (03:00pm) 1Q 2.8 %q/q	27 Feb Australia: Construction work done (11:30am) 4Q New Zealand: Building permits (10:45am) Jan 8.0 %m/m, nsa NBNZ business conf. (03:00pm) Feb -25 %bal	28 Feb Australia: Private capital expenditure (11:30am) 4Q 16.1 %oya New Zealand: Visitor arrivals (10:45am) Jan Money supply (03:00pm) Jan	29 Feb Australia: Private sector credit (11:30am) Jan 1.0 %m/m, sa New Zealand: Trade balance (10:45am) Jan -100 NZ$ mn
3 Mar Australia: Inventories (11:30am) 4Q Company profits (11:30am) 4Q RBA comm. index (04:30pm) Feb	4 Mar Australia: Current account (11:30am) 4Q Retail sales (11:30am) Jan RBA cash target (02:30pm) Mar New Zealand: ANZ commodity price (03:00pm) Feb	5 Mar Australia: GDP (11:30am) 4Q	6 Mar Australia: Trade balance (11:30am) Jan Building approvals (11:30am) Jan Indonesia: New Zealand: RBNZ official cash rate (09:00am) Feb	7 Mar Australia: Foreign reserves (04:30pm) Feb
10 Mar Australia: ANZ job advertisements (11:30am) Feb New homes sales Jan New Zealand: QV house prices Feb	11 Mar Australia: Housing finance (11:30am) Jan	12 Mar Australia: Westpac consumer confidence (10:30am) Mar	13 Mar Australia: Unemployment rate (11:30am) Feb New Zealand: Retail sales (10:45am) Jan PMI (12:00pm) Feb	14 Mar New Zealand: Mfg. activity (10:45am) 4Q
17 Mar	18 Mar	19 Mar Australia: BoP imports prelim. (11:30am) Feb WMI leading index (11:30am) Jan New Zealand: Credit card spending (03:00pm) Feb	20 Mar Australia: Motor vehicles sales (11:30am)Feb New Zealand: Visitor arrivals (10:45am) Feb	21 Mar *Holiday Australia,,New Zealand*

Highlighted data are scheduled for release on or after the date shown. Times shown are local.

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Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
25 - 29 Feb	25 Feb	26 Feb	27 Feb	28 Feb	29 Feb
	Euro area • Trichet speech Hungary • NBH meeting Malaysia • BNM meeting United States • Existing home sales (Jan)	Canada: Payrolls (Dec) Germany • GDP final (4Q) • IFO bus survey (Feb) Italy: ISAE bus survey (Feb) Japan • Shoko Chukin small bus survey (Feb) Slovak Republic • NBS meeting Taiwan • Export orders, IP (Jan) United States • OFHEO HPI (4Q) • PPI (Jan) • S&P/C-S HPI (Dec, 4Q)	Euro area • M3 (Jan) Poland • NBP meeting Thailand • BoT meeting United Kingdom • GDP prelim (4Q) United States • Durable goods (Jan) • New home sales (Jan) • Bernanke delivers semiannual monetary policy report to Congress	Euro area • Trichet speech Germany • CPI 6 states and prelim (Feb) • Employment (Jan) • Unemployment (Feb) Japan • IP prelim (Jan) • Retail sales (Jan) United States • GDP prelim (4Q) • Bernanke delivers semiannual monetary policy report to Congress	Euro area • EC bus survey (Feb) • HICP final (Jan) • Unemployment (Jan) Germany • CPI final (Jan) • Retail sales (Jan) Japan • Core CPI (Jan) • Household spend (Jan) • Housing starts (Jan) • PMI mfg (Feb) • Unemployment rate (Jan) Sweden: GDP (4Q) United Kingdom • Nationwide HPI (Feb) United States • Chicago bus surv (Feb) • Cons sent final (Feb) • Personal income (Jan)
3 - 7 Mar	3 Mar	4 Mar	5 Mar	6 Mar	7 Mar
Japan • Cabinet Office private consumption index (Jan) United Kingdom • Halifax HPI (Feb)	Canada • Real GDP (4Q) China • PMI mfg (Feb) Euro area • HICP flash (Feb) • PMI mfg final (Feb) Korea • CPI (Feb) • Trade balance (Feb) United Kingdom • PMI mfg (Feb) United States • Construction spend (Jan) • ISM mfg (Feb) • Light vehicle sales (Feb)	Australia • RBA meeting Canada • BoC meeting Euro area • GDP prelim (4Q) Korea • IP (Jan) Singapore • PMI mfg (Feb) United States • Bernanke speech	Australia: GDP (4Q) Brazil • IP (Jan) • COPOM meeting Euro area • PMI services final (Feb) • Retail sales (Jan) Japan: MoF corp surv (4Q) Taiwan: CPI (Feb) UK: PMI services (Feb) United States • ADP employment (Feb) • Beige book • Factory orders (Jan) • ISM nonmfg (Feb) • Prod and costs (4Q)	Germany • Mfg orders (Jan) Canada • Ivey PMI (Feb) United States • Pending home sales (Jan) Central bank meetings • Euro area • Indonesia • New Zealand • United Kingdom	Germany • IP (Jan) Japan • BoJ meeting Taiwan • Trade balance (Feb) United States • Consumer credit (Jan) • Employment report (Feb)

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